

## FUTURE CHALLENGE OF KNOWLEDGE TRANSFER IN SHARIAH COMPLIANCE BUSINESS INSTITUTIONS

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### ABSTRACT

The rapid growth of the global halal market makes a positive impact on the development of shariah compliance business institutions. Although many sectors are now involved in the halal business, there is a challenge in understanding how shariah knowledge can assist in the present business environment. Specifically, shariah compliance business institutions that involve in the halal business is required to develop their performance and competitiveness, but the rigid tacit knowledge of shariah knowledge may influence the business. To compete and deal with innovations in a complex and competitive situation, formulation of shariah knowledge transfer into explicit knowledge is required. This, in turn, will ease the distribution of shariah knowledge throughout the whole institution structure. The knowledge distribution also can lead to a better understanding as well as to lead to group performance and innovations. The purpose of this conceptual paper is to provide some insights on how shariah knowledge from the shariah board can be transferred, through standards officer, to the whole organizational structure, which, in turn, may help the team to improve company's performance.

**Keywords:** *knowledge transfer, Islamic corporate governance, group dynamics, team performance, competitive advantage*

### INTRODUCTION

It is estimated halal market that was spent by 1.8 billion Muslims around the world is worth US\$ 2.1 trillion in 2017. The most benefited sectors by the growth of the global halal market are (1) halal food, (2) Islamic finance, (3) halal travel, (4) modest fashion, (5) media and recreation, (6) pharmaceuticals and cosmetics. There are also trends that motivated global market related with ethical economy, especially with shariah compliance is that relevant on this issue, which are: (1) ethical consumption or investment, (2) government ethical regulation, (3) faith-based trends, (4) ethical market profit (Thomson Reuters 2018).

Understanding halal ecosystem penetration in the global market, which is dynamic, is covering infrastructures of business networks and involving governmental or non-governmental institutions. This halal global market start from Islamic finance and its

expansion to global business industries increase demand from global Muslim communities and market about shariah compliance product and services (BNM 2015).

This fascinating growth of the global halal market will give a big impact on the halal business, many shariah compliance business institutions will flourish and take a positive role in this business. In global market halal business, which not only can be done by Muslims, many of corporation will invest to learn and adapting approach how to make their business shariah compliance.

This paper is trying to give an alternative on how shariah knowledge needs to distribute on whole company authority's employer not only stay in shariah board or top management to face the future challenge of shariah compliance business institutions in the global competitive market that demand more of innovations and understanding of shariah knowledge.

## **SHARIAH KNOWLEDGE AND FUTURE CHALLENGES**

### **Knowledge Transfer and Inclusivity**

Organization learning is learning from their experience, even in the global market competition they also learn from their competitors or another organization. The form of learning is affected by some factors: structure, culture, resources, goals, feedback system, power distribution, training system, and another hidden internal condition. Hierarchy structures on a formalization of specialty that not necessary vertical structures are increasing capability of organization learning, while vertical integration which consists of ordinate and sub-ordinate is slowing down the learning process (Argote 2014).

There are also some category of issues that related with knowledge transfer that need to considerate, which are: (1) network structure, (2) generic issue, (3) social issue, (4) language, (5) organizational aspect, and (6) technical issue (Bellini, Aarseth, & Hosseini 2016). From it, we can understand the issue of knowledge transfer in shariah compliance business institutions is not just about the knowledge itself but also structure and distance between actors and authority holder or shariah boards.

Other research also supports this argument and give some engineered solution on how to use knowledge transfer as tools and get a result from it. This research mentions the other factors that influence innovations and creativity are the inclusivity of knowledge sharing. There is an engineered approach to accumulated knowledge and relevant authority indirect actors, so they can come with ideas and solutions (Kremer, Villamor, & Aguinis 2019).

### **Shariah Compliance and its Advantages**

Shariah compliance economic activities is attributed by several features: (1) estimating by real value, (2) every contract is a direct peer-to-peer transaction, (3) assurance of product information or services, (4) clear agreement about profit or loss (Tatiana, Igor, & Liliya, 2015). There is also a major issue that tackled on shariah compliance, which are (1) riba' or usury or interest, (2) maysir or gambling, (3) gharar or uncertainty, and (4) haram or forbidden (Adam & Bakar 2014; F. Khan 2010). All of these features and major issues were discussed in shariah knowledge, along with their derivatives and forms on the present condition.

Some scholars argue that Islamic Banking and Finance, as the most matured sectors of the global halal market, actually just a same with the conventional banking system, and

what makes it different is on the transaction which the contract is documented and agreed as a mutual benefit (F. Khan 2010). Another research also showed the competency of shariah compliance business institutions is shown on how they affected by the crisis, there is some evidence that the approach of shariah compliance is higher on capitalization and asset quality (Beck, Demirguc-Kunt & Merrouche 2013).

Two mechanisms that worked in governance institutions: internal mechanism and external mechanism, and there are some differences of mechanism worked in general corporate governance, bank governance, and Islamic banking governance. In the scope of the internal mechanism, Islamic banking governance has addition than general corporate governance, Islamic banking governance as the addition of shariah supervisory boards, the shariah review unit and the Islamic Financial Services Board (IFSB) as the main mechanism to monitoring. In the scope of external mechanism, Islamic banking governance involving the participation of public policy institutions, regulatory and supervisory authorities, and shariah authorities. This mechanism playing a significant role in Islamic banking governance (Ben Bouheni, Ammi, & Levy 2016). As the most matured shariah compliance business institutions, the mechanism of Islamic banking governance is generally adopted in most shariah compliance business institutions' practices.

Even though, there is still a concern on how the shariah compliance approach can influence business and industry practices in any other sectors besides Islamic Banking Finance. For example sectors that still have a lot spaces to explore, such as: waqf governance (Abd Ghadas & Abd Aziz 2017; Harasani 2015; Mohsin et al. 2016), halal supply chain (Ali, Tan, & Makbul 2013; M. I. Khan, Haleem, & Khan 2018; Qurtubi & Kusrini 2018), Islamic work ethics (J. Ali 1988, 2015; Mohammad et al. 2018; Salahudin et al. 2016), and any other sectors related.

### **Shariah Knowledge: Islamic Ethics, Fatwa and Understanding**

Islamic ethics is the principle right and wrong based on the thought of the Quran and Hadiths. Before we need to understand that there is a different understanding between law and ethics, even in general public have difficulties to distinguish both. Ethic also cannot be understanding subjectively or based on cultures, ethic is standing for what is fundamentally good (Abdurezak A. Hashi 2011). Research has shown Islamic ethics have a great influence on working commitment of employee and is also shown that employee who has understanding having more loyalty to organization generally (Salahudin et al. 2016).

The fatwa on another hand is complementary to ethics. It is an explanation by scholars in detail about something that does not have clarification in the Quran and Hadiths. The main concept of mechanism how fatwa can be produced is through ijтиhad, which means responsible analyst referred to the Quran, Hadiths, and considering previous fatwa or previous understanding by scholars. By the time there is also some evolution on who fatwa resulted, from individual scholars, authority institutions or by consensus of scholars (Abbas 2015; Hisyam et al. 2017; Mamat 2019).

"Understanding shariah" or Ittiba' is more on the actor side when activities are made, so it is an individual activity to understanding ethics and fatwa, and this activity is the fundamental attitude that needs to be possessed by every individual (Abbas 2015). Of course, there will be a lot of different understanding on some issues, which is normal because we as an actor have different perspective and condition faced as consideration.

## **Formulating Shariah Knowledge Into Explicit Knowledge**

Tacit knowledge is identified as the knowledge that difficult to standardize and just can be explored when it practices (Kogut & Zandes 1992). Some knowledge has difficulties to transfer, these attributes called knowledge tacitness, and it also depends on where the knowledge transfer occurs, is it on intergroup or intragroup (Nakauchi, Washburn, & Klein 2017). On the other hand, explicit knowledge is the knowledge that can be standardized or documented, this kind of knowledge is easy to transfer and communicate (Grant 1996).

By taking this tacit and explicit knowledge description we can assume ethics and fatwa which now days was issued by either authorities, council or a recognized association are well-documented knowledge or explicit knowledge along with another standard. Also different from ethics and fatwa knowledge, with the expansion of shariah compliance business activities in many other sectors, it is needed the practical understanding-shariah knowledge on the ground field collaborating along with their professional or technical knowledge. In simple words by this, we can easier to adapt shariah compliance business activities in the global market and industries so it can give more innovations and better performances.

## **Future Challenges**

While we enthusiast on how global halal market growing, there are some sentiments of uncertainty in the global economy with isolation and protection policies. There are trends on socio-economic in Islamic economic, that selected from four socio-economic indicators: (1) economic outlook, (2) poverty and health, (3) education and empowerment, and (4) infrastructure (IsDB 2018).

With many sectors will involve in the global halal market, there is also a positive demand for shariah compliance business institutions not only producing halal products but also halal on the process, green, ethical, socially responsible and have good services impression (Zain, Darus & Ramli 2015). With all this present condition and challenges, furthermore expansion of the Islamic approach to another global market sector that we can generalize as shariah compliance business institution in the global halal market, it is necessary to adopt some approach that suitable enough to assist this expansion (Yaacob & Abdullah 2013).

## **STRUCTURES AND PERFORMANCE**

### **Shariah Boards & Human Capital Gap of Knowledge**

Shariah boards or known as shariah supervisory boards are top management structures that involved with authorities to decide and function as a gatekeeper for an institution to ensure of sharia-compliant practices (Hashim, Mahadi & Amran 2015). The shariah boards are playing a vital role in screening shariah compliance business activities. However, it is still needed manual screening analysis to ensure shariah compliance activities (Adam & Bakar 2014). Shariah boards position in the hierarchy is the same level as board commissioner (Indrawaty & Wardayati 2016). Even more, shariah supervision boards can be seen as the main structures that differencing from conventional business institutions (DeLorenzo 2012; Ginena & Hamid 2015). More important in the emerging environment, shariah boards are seen as the credibility of shariah compliance institutions (Malkawi 2013; Wardhani & Arshad 2012).

In Islamic banking governance, there are units called shariah reviews units that have a secondary task to monitoring complementary of shariah boards (Ben Bouheni et al. 2016). But, to adapt to general shariah compliance business practices which are not just related to financial basis activities, it needs more than shariah reviews unit. In practice, the knowledge gap and limited authorities of shariah review units, make serious problems in shariah compliance governance (Bahari & Akhtar Baharudin 2016).

With many sectors will approach the global halal market, we can see there are some difficulties by micro-finance, start-up or SME to setting up shariah boards in terms of quality and practicality (Mande 2015). Research that involves two well-established fully-fledged Malaysian Islamic banks also finds sharia compliance business institutions sharia boards, does not give an effective impact on the good performance of the company, except boards that have professional expertise (Haridan, Hassan, & Karbhari 2018; Ramli & Ramli 2016). This indicates that to have qualified board members that know with shariah knowledge is just not enough. Furthermore, it also needs professional skills to get collaborated knowledge so it can benefit company performance.

### **Shariah Internal Control**

Shariah reviews unit is categorized as an internal audit because it has function and scope authority like an internal audit process. Audits can be described as an analysis and evaluation activities to find out the information in compliance with the standard required (Daniela & Attila 2013). Shariah reviews unit have the authority to observe such activities is shariah compliance or not, but they do not have the authority to choose, change or stop activities that are not shariah compliance.

What we need in this case is an authority not only to reviews but also change and improve activities that are not fully fill shariah compliance requirements in the ground field itself. They need to have the knowledge and practical ability, and they also facing directly the issues, so they can understand the situation and condition more comprehensive. Similar with big and medium institutions, a small-medium enterprises, start-up, small shariah compliance business institutions, it is beneficial to formalized internal control practices in every level of activities in order to identify and investigate the activities is shariah compliance directly (Mohamed et al. 2014; Sanusi et al. 2015).

In our consideration, it is also important to formalized standards officer as internal control, but it does not mean that we not audit for shariah compliance activities. An internal or external audit can be conducted, what this paper what to address is the function of internal control is necessary because direct in charge with the main activities of producing product or services, to provide better assurance of shariah compliance.

### **Distributed Knowledge, Innovations and Performance**

The combination of explicit knowledge and tacit knowledge also related to local and geographical basis will create innovations (Roper, Love & Bonner 2017). It is what we want also in shariah compliance business institutions, the potentials and possibility of shariah compliance to penetrating the new market is dependent on the combination of knowledge of ethics, fatwa, and "understanding-shariah" of actors that facing the ground field. This combination and integration of knowledge are being the competitive advantage of shariah compliance business institutions.

In delivering products, enhancing quality and standard needs by customers, the knowledge management processes (absorptive capacity, knowledge transfer and knowledge

application) will give impact to customer value (Cepeda-Carrion et al. 2017). By this understanding, having a shariah knowledge and "understanding-shariah" in the field also supported with relevant authority can improve customer value. It is also supported by on how innovations can occur easier when interacting with clients or facing the problems in the field, this external influence can be seen as innovation intermediaries (Coursey et al. 2019; De Silva, Howells, & Meyer 2018).

There is also an empirical study on how Islamic work ethics influenced the team performance, how these ethical values related to psychological ownership and attitudes resulted in a constructive, positive, optimistic work climate environment (Mohammad et al. 2018). In general, there is also correlation on how shariah compliance business practices have an impact on long-term financial performance (Pepis & de Jong 2019). Also "understanding-shariah" knowledge as tacit knowledge that even identifies with its difficulty to transfer it also has a significant contribution to organizational performance (Muthuveloo, Shanmugam & Teoh 2017).

## CONCLUSION

As shariah compliance business institutions really rely on how the practices and activities of industry in the global market is shariah compliance, it is necessary to identify the knowledge of shariah (ethics, fatwa) as explicit knowledge that already standardize by authorities, while understanding how to implement and deal with activities is as tacit knowledge, and because of differences of capabilities of each worker, we can see it as a competitive advantage of industries in the global halal market environment.

Knowledge transfer and inclusivity of authorities are needed and it can be seen in the formalization of internal control that has the capability not only review shariah compliance but also "understanding-shariah" knowledge as standards of quality in their ground field of activities that can deliver more innovations and better performance.

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